MODIFICATION OF PUBLIC CONTRACT: BETWEEN RULE OF FAIR COMPETITION AND FREEDOM OF CONTRACT PRINCIPLE

Theodora Pritadianing Saputri
Fakultas Hukum, Universitas Katolik Parahyangan, Bandung
email: theosaputri@unpar.ac.id

disampaikan 10/10/18 – di-*review* 24/11/18 – diterima 22/12/18
DOI: 10.25123/vej.3035

Abstract
It is internationally accepted that public procurement procedure and public contract shall be organized in accordance with the fair competition principle and fulfil the requirement of transparency. Public procurement regulations are necessary to secure the efficient use of taxpayer resources by the government in purchasing goods, services and works from the market and to ensure fair competition among the public contract should be protected and that therefore it would be necessary to amend existing regulations which prohibit or restrict this right derived from freedom of contract. In addition, law makers should also put in place restriction with regard to corporate restructuring which main intention is to circumvent requirements of tender documents.

Keywords:
public procurement, public contract, fair competition, parties' autonomy, modification of public contract.

Abstrak
Telah diterima secara internasional bahwa prosedur pengadaan barang dan jasa pemerintah dan kontrak bersama pemerintah harus dilaksanakan sesuai dengan prinsip persaingan usaha yang sehat dan memenuhi persyaratan transparansi. Peraturan pengadaan barang dan jasa pemerintah diperlukan untuk melindungi penggunaan yang efisien dari dana pajak oleh pemerintah dalam melakukan pembelian barang, jasa dan pekerjaan lain dari pasar barang dan/atau jasa dan untuk memastikan persaingan usaha yang sehat antara pelaku bisnis yang terlibat. Peraturan pengadaan barang dan jasa pemerintah di Indonesia mengatur kriteria-kriteria yang membatasi kebebasan para pihak untuk mengubah kontrak bersama pemerintah yang pada umumnya diadakan melalui proses lelang yang kompetitif. Berkenaan dengan itu tulisan ini akan membahas persoalan seberapa jauh asas kebebasan berkontrak ini dapat dilaksanakan jika kita berhadapan dengan kontrak-kontrak public. Pandangan utama penulis di sini ialah bahwa pembuat undang-undang perlu tetap menghormati kebebasan berkontrak ini dan sekaligus mengatur batasan yang lebih baik. Selain itu diargumentasikan pula bahwa alasan restrukturisasi perusahaan untuk mengubah kontrak perlu diatur dan dibatasi.

Kata Kunci:
pengadaan barang dan jasa, kontrak pemerintah, persaingan usaha yang sehat, kebebasan berkontrak, perubahan terhadap kontrak pemerintah.

Introduction

In the act of a public procurement, the government makes a purchase to carry out a particular function,[1] for instance to improve the mobility access to the public by procuring the construction of a road toll. Public expenditure on goods, services and other works represents an average of 13 per cent of GDP in OECD (Organization for Economic Cooperation and Development) countries.[2] In Indonesia, the government allocates approximately 30 per cent of the annual state's budget in each year for expenditure on public procurement.[3]

The basic concept of public procurement is that the money held and spent by the government is public money, which effectively belongs to citizens and is held for them in trust by government, to be spent in a proper manner which includes delivering value for this money.[4] In addition, the government shall distribute public money to economic operators through a transparent process and in a competitive environment. Otherwise, the government may deliver excess market power to certain economic operators which can lead into long-term discrepancies between number of supplier and user and affect cost of public procurement by the relevant contracting agencies. If the public procurement process is executed in accordance with the legal framework, the government may achieve its public objectives such as the reduction of unemployment or support for industries, trades, or disadvantaged groups.[5] Thus, regulations on public procurement are necessary to achieve the efficient use of public money and ensure the implementation of fair competition principle.

On fair competition principle, *Black's Law Dictionary* defines competition as follow:[6]

---

1 S. Arrowsmith & P. Kunzlik, Social and Environmental Policies in EC Procurement Law: New Directives and New Directions, Cambridge University Press, Cambridge, 2009, at 13.

2 OECD Government at a Glance 2013, on which see A. Semple, A Practical Guide to Public Procurement, Oxford University Press, Oxford, 2015, at xxxiii.

3 S. N. Bahagia, Sistem pengadaan publik dan cakupannya, 1 Senarai Pengadaan Barang/Jasa Pemerintah, 2011, at 10.

4 S. Arrowsmith, The Law of Public and Utilities Procurement Regulation in The EU and UK, 3rd ed., Vol. I, Sweet & Maxwell, London, 2014, at 21.

5 OECD Government at a Glance 2013, on which see A. Semple, *supra note* 2, at xxxviii.

6 Black Law Dictionary (fifth edition). St Paul Minn West Publishing CO 1979, at 86.

> "Competition: contest of two rival. The effort of two or more parties, acting independently, to secure the business of a third party by the effort of the most favorite term; also the relation between different buyers or different sellers which result from his effort. It is the struggle between rivals for the same trade at the same time; the act of seeking or endeavoring to gain what another is endeavoring to gain the same time. The term implies the idea of endeavoring by two or more to obtain the same object or result."

While unfair competition as defined in Law No. 5 of 1999 is competition between economic operators which is carried out in dishonest manner, unlawful method and impairing fair competition.[7] With respect to competitive procedure or tender, Article 22 of Law No. 5 of 1999 as revised by the Constitutional Court by virtue of its decision No. 85/PUU-XIV/2016 dated 20 September 2017 stipulates that economic operators shall not commit a collusive behavior (collusive tendering or bid rigging) with other economic operators and/or affiliates of other economic operators to arrange and/or to determine the winning bidder which leads into unfair competition. Bearing in mind the objectives of public procurement which, amongst others, is to evenly distribute public money and market power to economic operators, government must ensure that public contract shall not be easily modified which may cause the granting of excess market power to certain economic operators. In addition, without ensuring fair competition between economic operators the government will fail to obtain the contract with the best value for money, which in turn will reduce the efficient use of public funds.

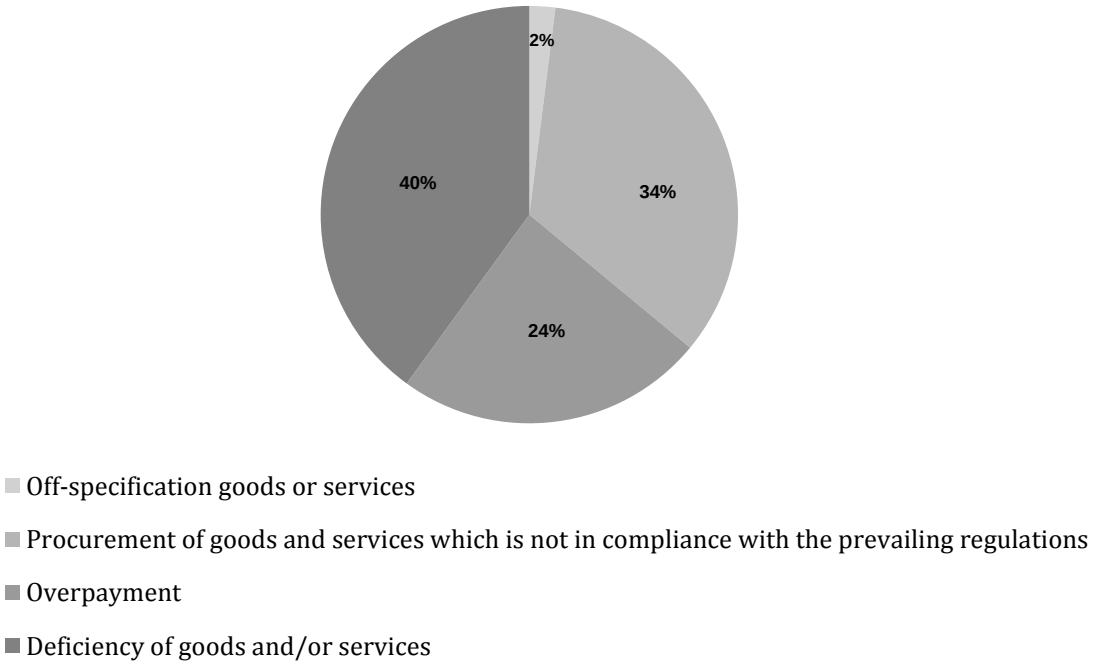
Regulations on public procurement usually contains list of rigid procedures to be followed by the contracting agencies and the economic operators. Most countries have the tendency to control the contract award procedure to obtain contract with best value for money and engage qualified economic operators. There are clear legal consequences for any deviations in the contract award procedure. The question arises whether it is sufficient only to control the contract award procedure or whether it is also necessary to control the contract management phase. We will see in section V below how Indonesian public

---

7 Law of the Republic of Indonesia Number 5 of 1999 concerning Anti-Monopoly and Unfair Competition dated 5 March 1999 as published in the Staatsblad (Law Gazette) No. 33 of 1999 ("**Law 5/1999**"), at article 1 (6).

procurement regulations control the implementation phase of a public contract including modification to the terms and conditions of a public contract. Nevertheless, it seems that despite the rigid regulations in public procurement sector, State Audit Board (*Badan Pemeriksa Keuangan,* "**BPK**") of the Republic of Indonesia found that there were several cases where modification of an agreed public contract, *inter alia*, by receiving goods or services of a lower quality than those that had been approved, or in the amount less than had been previously agreed, have caused State financial losses. Below is the information on BPK's findings on public procurement cases that was published by LKPP in the first half of 2016:[8]

Procurement Cases Causing Financial Losses to the Government Identified by BPK in 2016



State financial losses may be avoided or justified if there is a clear regulation or limitation with regards to the modification of public contract.

8 Badan Pemeriksa Keuangan, Ikhtisar Hasil Pemeriksaan Semester I Tahun 2016 at Table 1.5 & Table 2.5, available at http://www.bpk.go.id/assets/files/ihps/2016/I/ihps_i_2016_1475566035.pdf, and last visited (09-10-2018).

Other than BPK's finding, there are several circumstances that may infringe fair competition principle in the implementation of public contract. First, in the event of situation whereby the contracting authorities require the initial contractor to provide additional services, supplies, or works which are not part of the initial contract. Second, a replacement of the initial contractor which may be resulted from a corporate restructuring. In those cases, the government must provide safeguard and limitation on the modification of public contract. Hence, modification of public contract will not lead into unfair competition amongst the economic operators.

On the other hand, many countries adopt a general principle in contract law that each party to a contract shall have party's autonomy and free to amend the contract with the consent of its counter party. We know this general principle as freedom of contract principle. It should be noted that if party's autonomy is the only restriction, the parties could easily undertake necessary measures to resolve unforeseen circumstances which occur during the performance of the contract.[9] It is indeed true that a public contract is still a contract and the involved parties shall have parties' autonomy. However, bearing in mind that a public contract is awarded through a rigid competitive procedure, parties' autonomy in a public contract may need certain limitations.

Main question that would be explored in this paper is to what extent the regulation may restrict freedom of contract principle and how the regulation should be drafted in a way that modification of public contract will not result in unfair competition amongst the economic operators. Public contract in this paper shall refer to contracts for services and/or goods that are awarded through a competitive procedure under the public procurement regulations including Presidential Regulation Number 16 of 2018 and its implementing regulations, Construction Law Number 2 of 2017 and PTK-007/SKKMA0000/2017/S0, which includes Technical Guidance for the Procurement of Goods and Service in the oil and gas sector. This paper shall examine conditions that must be met for

9 R. D. Olivera, Modification of Public Contracts Transposition and Interpretation of the New EU Directives, 10 EPPPL, 2015, at 35.

modifications of a public contract under the Indonesian regulations in public procurements sector and how should we restrict parties' autonomy in a public contract without violating the general principle in contract law.

Analysis

Freedom of Contract

Party's autonomy (self-determination) or freedom of contract is one of the general principles in contract law which is recognized not only in Indonesia but in most of countries. In Indonesia, there is no regulation that explicitly explain the meaning of freedom of contract principle. Nevertheless, article 1338 of the Indonesian Civil Code stipulates that every contract that is made and entered into by the parties in accordance with the prevailing laws and regulations shall be binding and enforceable to the parties. According to the freedom of contract principle, anybody is free to enter into a contract with any person of his choice, free to determine the content of the contract, and to choose the form of contract even the governing law of the agreement.[10]

Referring to the freedom of contract principle, parties to a public contract shall have the right to modify the content of the contract in order to overcome any unforeseen circumstances. Nevertheless, attention should be drawn to article 1338 of the Indonesian Civil Code stating that the contract must be in accordance with the prevailing laws and regulations. Therefore, freedom of contract should be restricted by the applicable laws and regulations including those in relation with fair competition principle.

As has been mentioned in Section I above, there are circumstances in relation with modification of public contract that will infringe fair competition principle. Those are replacement of initial contractor and also granting of additional scope of work for the contractor. Ideally, the winning bidder shall not be replaced by third party without going through the competitive procedure. This is to ensure that the losing bidders have the same opportunity to be chosen as new

[10] Arthur S. Hartkamp et al., Contract Law in the Netherlands, Kluwer Law International, The Netherlands, 2011, at 34.

contractor. The same applies to additional scope of works. Additional scope of works must be tendered by the government to guarantee fair competition amongst the economic operators. However, if all matters must be re-tendered, cost and time for re-tender process may adversely affect the government. Therefore, freedom of contract must still be regarded as one of important principle in modifying public contract.

Reasons to Justify Certain Form of Modification of Public Contract

As mentioned in Section I and Section II A above, the principle of fair competition may be infringed during the execution of the contract because of the lack of proper contractual management.[11] Where the contract is not managed in a proper way, the agreement can be reached on a lower level of quality than that which was originally promised, and can be accepted by the contracting authorities in contrast with the contract provision.[12] The acceptance of the awardee's lower promise makes it appear as if the contracting authority has failed to choose the best tender.[13] In such cases, the former unsuccessful tenderers may challenge the contracting authority on the basis that a full and open competition had not been assured.[14]

Changes or deviations during the execution of the contract might distort competition and infringe upon the rights of the losing tenderers.[15] Furthermore, if the contract that has been awarded can be changed later, there is a risk that national firms, in collusion with the contracting authority or otherwise, may be

---

11 G.M. Racca and R.C. Perin, Material changes in contract management as symptoms of corruption: a comparison between EU and U.S. procurement systems, in G.M Racca and C.R. Yukins (Ed.), Integrity and Efficiency in Sustainable Public Contracts Balancing Corruption Concerns in Public Procurement Internationally, Bruxelles, 2014, at 255.

12 *Id*, at 252.

13 See F. J. Vazquez Matilla, The modification of public contract: an obstacle to transparency and efficiency, in G.M Racca and C.R. Yukins (Ed.), Integrity and Efficiency in Sustainable Public Contracts Balancing Corruption Concerns in Public Procurement Internationally, Bruxelles, 2014, at 294.

14 *Id*.

15 G.M. Racca, et al., Competition in the Execution Phase of Public Procurement, 41 Public Contract Law Journal, 2011, at 90.

able to obtain an advantage in the award procedure by tendering favorable terms in the expectation that they will be changed after conclusion of the contract.[16]

One of the defences made for the modification of a public contract relates to the difficulties and detrimental consequences that attend upon retendering the contract. An efficient government procurement system must endeavour to attain the highest possible value for money.[17] As mentioned earlier, the government may not be able to demonstrate the highest possible value for money in the retendering procedure. If the terms and conditions of a public contract are no longer compatible with the purpose of the contract for whatever reason, the government may have three options at its disposal.[18] First, it can continue the contract without any amendment, which is likely to be inefficient, and which carries the risk that the contract might not be able to meet the needs of the government.[19] Second, it can terminate the contract and initiate a new tendering procedure, which will translate into a loss of time and significant delays that have detrimental consequences for the public interest, and which may implicate the government as responsible and liable to compensation for the contractor as a result of the termination of the contract.[20] Third, it can modify the contract so that it serves the needs of the government. The third option may become the most efficient option in many cases.[21]

Nevertheless, aside from distortion of competition in the procurement market, presenting discretion to contracting authorities to modify a contract may lead to corruption during the tendering procedure and execution of the contract's modification.[22] Hence, it is important to establish rules of law that will narrow the discretion of contracting authorities to agree on the modification of a public contract after it has been awarded. In Indonesia, the modification of a public

---

16 S. Arrowsmith, *supra note* 4, at 578.
17 G.M. Racca, et al., *supra note* 15, at 94.
18 O. Dekel, Modification of A Government Contract Awarded Following A Competitive Procedure, 38 Public Contract Law Journal, 2009, at 406-407.
19 *Id*, at 407.
20 See R. D. Olivera, S*upra note* 9, at 37.
21 O. Dekel, *supra note* 18, at 407.
22 G.M. Racca and R.C. Perin, Material Amendments of Public Contracts During Their Term: From Violations of Competition to Symptoms of Corruption, 8 EPPPL, 2013, at 291.

contract is restricted by Indonesian procurement law as will be elaborated in Section C and D below.

General Overview Indonesian Procurement Law

Generally, the public procurement rules in Indonesia are stipulated in Presidential Regulation Number 54 of 2010 concerning the Procurement of Government Goods and Services,[23] as recently replaced with Presidential Regulation Number 16 of 2018 concerning the Procurement of Government Goods and Services.[24] PR 16/2018 defines public procurement as the activities carried out by ministries/agencies/working units/institutions to acquire goods and/or services by using the state's budget and/or the budget of regional government covering the planning stage until the completed acquisition of the required goods and/or services.[25] Goods in PR 16/2018 is defined as tangible and intangible, movable and immovable, goods for commercial use, and consumable goods.[26] The term "services" shall include construction work, consultation services, and other services requiring skill ware.[27]

For upstream oil and gas sectors, although the goods and/or services are purchased by upstream oil and gas companies which are private entities, there are similar, but more specific, procurement rules that must be complied with by these private entities. The procurement rules for upstream oil and gas companies are contained in the PTK-007/SKKMA0000/2017/S0, which includes Technical Guidance for the Procurement of Goods and Service in the oil and gas sector ("**PTK**

---

23 Presidential Regulation of the Republic of Indonesia Number 54 of 2010 on the Procurement of Government Goods and Services as amended by Presidential Regulation of the Republic of Indonesia Number 35 of 2011, PR 70/2012, Presidential Regulation of the Republic of Indonesia Number 172 of 2014 and lastly Presidential Regulation of the Republic of Indonesia Number 4 of 2015 ("**PR 54/2010**").

24 Presidential Regulation of the Republic of Indonesia Number 16 of 2018 on the Procurement of Government Goods and Services dated 22 March 2018 as published in the Staatsblad (Law Gazette) No. 33 of 2018 ("**PR 16/2018**").

25 PR 16/2018, article 1 paragraph (1).

26 *Id*, Article 1 paragraph (29).

27 *Id*, Article 1 paragraph (30), (31) & (32).

007").[28] This Guidance is issued by the Special Task Force for Upstream Oil and Gas Business Activities ("**SKK Migas**"), formerly known as BP Migas. The government of Indonesia imposes these procurement rules to the upstream oil and gas companies because there is a cost recovery system in place in the upstream oil and gas sector. Pursuant to this system, the exploitation cost of the upstream oil and gas companies will be recovered by the government from the sale of oil and gas extracted from the relevant oil and gas fields on an annual basis. It is important to discuss the provisions concerning the modification of a contract that is awarded through a competitive procedure under the PTK 007, since PTK 007 contains more detailed rules on the modification of the contract awarded through a competitive procedure.

In addition to the SKK Migas rule, there is another sectoral regulation that might have an impact on the execution of a public contract relating to construction works, which is the Law 2/2017. The Law 2/2017 replaced the old Indonesian Construction Law No. 18 of 1999. However, the implementing regulations of the old Indonesian Construction Law, such as government regulation No. 29 of 2000 on the Construction Services ("**GR 29/2000**") as amended from time to time, shall remain valid to the extent that the provisions under those implementing regulations do not stand as contrary to the provisions under the Law 2/2017. The Law 2/2017 acknowledges that the contract for a construction project which is funded with the state's budget must be awarded through a competitive procedure in accordance with the prevailing regulations on public procurement.[29]

PR 54/2010, the old public procurement regulation, emphasizes the prohibition against unfair competition through collusive tendering which can be identified from, among other things, the submission of similar technical documents from the tenderers, or participation of more than one entity within the

---

[28] PTK 007 consists of 5 books. Throughout this paper, the focus lies upon the Second Book of PTK 007, which covers the provision to do with the modification of a contract that is awarded through a competitive procedure.

[29] See the Law of the Republic of Indonesia Number 2 of 2017 concerning Construction Services dated 12 January 2017 as published in the Staatsblad (Law Gazette) No. 11 of 2017 ("**Law 2/2017**"), at article 42 (1).

same group companies in the tendering procedure.[30] Similar approach is used in PR 16/2018 as may be seen in Article 78 of PR 16/2018.

Requirements for the Modification of a Public Contract under Indonesian Regulations

Definition of Public Contract under the Public Procurement Regime

Article 1 (44) of PR 16/2018 describes public contract as written agreement between the contracting authority and private entity as supplier or service provider. For the purposes of clarity, and in accordance with the guidelines issued by the National Public Procurement Agency (*Lembaga Kebijakan Pengadaan Barang Jasa Pemerintah,* "**LKPP**") in 2018, a public contract may consist of the following documents:[31]

a) Contract agreement / *surat perjanjian*;
b) Letter of tender;
c) Special conditions of contract;
d) General conditions of contract;
e) Warranties which consist of advance payment bond, performance bond and maintenance bond; and
f) Guarantee certificate.

Accordingly, the modification of a public contract shall cover the modification of all above-mentioned documents.

1. Unforeseen Circumstances and Limitation to Modify Contract Price

PR 16/2018 stipulates the following:[32]

> *"(1)* In the event of any discrepancy between the site conditions, at the time of execution of the Contract Document, and the drawings/technical specifications specified in the Contract document, the Contracting Authorities together with the Contractor may agree to make changes to the Contract document which include the following:
> (a) to increase or decrease the volume of goods/services/works which are listed in the Contract document;
> (b) to add or reduce the types of services/works;

---

30 S. Ramli, Bacaan Wajib Mengatasi Aneka Masalah Teknis Pengadaan Barang/Jasa Pemerintah, Visimedia, Jakarta, 2014, at 196.

31 Regulation of the Head of National Public Procurement Agency of the Republic of Indonesia No. 9 of 2018 concerning Technical Guidance for the Procurement of Government Goods and Services ("**Perka LKPP 9/2018**"), at 14-22.

32 PR 16/2018, *supra note* 24, Article 54.

(c) to modify the technical specification to adjust with the actual field conditions; and/or
(d) to alter the schedule for the implementation of the Contract.

(2) If changes as mentioned in paragraph (1) cause increase in price, the increase in price shall not exceed 10% of the original contract price."

As may be seen from the Article 54 (1) of PR 16/2018 above, unforeseen circumstances, where a public contract can be amended, is limited to the discrepancy between the actual site conditions and the information contained in the Contract document. The given illustration of this circumstance is one in which the contracting authority organizing the tendering procedure for a construction work whilst the land clearing work that should be completed by the contracting authority is still formally an ongoing process.[33] In such event, the contractor may choose to rely on Article 54 (1) of PR 16/2018 and freedom of contract principle to negotiate the modification of terms and conditions of the relevant public contract. There are no other rules in PR 16/2018 that limits parties' discretion to modify public contract that will safeguard fair competition principle during the execution of the public contract.

Perka LKPP 9/2018 as implementing regulations of PR 16/2018 contains additional information with regards to modification of public contract. Pursuant to Perka LKPP 9/2018, a change to the Contract document which is required to rectify the administrative matters may be made upon the agreement between the Contracting Authorities and the Contractor. [34] Term "administrative matters" refers to change of address, change of bank account and any other administrative information. This additional rule does not have contribution in enforcing fair competition principle in modifying public contract.

Another question then arises how to act if there is change in law resulting in unfair position between the contracting authority and the contractor or where the central government decided to cut off the contracting authorities' budget for the current year. Neither PR 16/2018 nor Perka LKPP 9/2018 provides a clear answer to this question. According to freedom of contract principle, the parties

---

33 R. A. Suryo & A. M. Ulfa, Teori Kontrak dan Implikasinya terhadap Regulasi Pengadaan Barang/Jasa Pemerintah, 3 Jurnal Pengadaan, 2013, at 53.

34 See Perka LKPP 9/2018, *supra note* 31, at section 7.13.1.

must be allowed to renegotiate the terms and conditions of the relevant public contract. Nonetheless, if we refer to the answers from LKPP on the frequently asked question list, LKPP suggests that for a public contract with a unit price, the parties may agree to decrease the volume of goods/services/works which are listed in the contract.[35] For a lump sum public contract, LKPP suggests that any modification must be avoided except if it is not possible to continue the execution of the contract without modification. On that occasion, the parties are allowed to modify the volume of goods/services/works but are not allowed either to adjust the price or to change the scope of supplies/services/works which are stipulated in the contract.[36] From LKPP's answer, it seems that LKPP intends to guarantee that the winning bidder will not have the right to negotiate the contract price that had been approved in the tendering process. Hence, the losing bidder will not challenge that their price is lower than the winning bidder.

Another issue related to the issue of unforeseen circumstances is where (a) there are discrepancies between the actual result of a construction work and the planning document prepared by the consultant of the contracting authorities, provided that such discrepancies do not result from the contractor's negligence or omission; (b) in order to rectify such discrepancies, additional works must be done; and/or (c) the cost of the additional works exceeds the 10 per cent caps as stipulated in the PR 16/2018. Pursuant to provision in Article 54 (2) of PR 16/2018, if the increase in price exceeds the 10 per cent caps, the execution of the additional works must be opened for tender. Nevertheless, there is provision within the presidential regulation which states that a contractor may be directly appointed for a construction work, which constitutes a part of an inseparable construction system and where responsibility over a building failure risk resulting from an unforeseen condition can only be attached to the appointed contractor.[37] PR 16/2018 also allows direct appointment for certain cases such as procurement

---

35 Frequently Asked Question LKPP, available at https://www.scribd.com/document/248537528/tanya-jawab-pengadaan-lkpp-1-pdf, last visited (09-10-2018).

36 *Id*.

37 PR 16/2018, *supra note* 24, Article 38 paragraph (5) (c).

of goods and services by a patent holder.[38] In these cases, fair competition may be infringed because the winning bidder is granted with additional works and prices. To avoid unfair competition, government should notify all tenderers of the possibility to grant additional works and increase in contract price. Therefore, transparency must be applied to guarantee the implementation of fair competition.

The Law 2/2017 does not include any specific rules relating to the modification of a construction work contract in the case of unforeseen circumstances. However, the implementing regulation of the old construction law, which is GR 29/2010, regulates that for a lump sum contract the contract price must be fixed and all risks that occur during the execution of the contract shall be borne by the contractor unless there is change of drawing and specification.[39] This rule can be translated as allowing for price adjustment where there is a change to the drawing and specification that have been agreed already. If this rule is interpreted broadly, the parties may argue that they have the right to modify construction contract without any limitation even though the contract was granted through a competitive procedure. Hence, there is a necessity to amend this rule.

There is a specific section in the PTK 007 about change of contract price and change of scope of works/services/supplies.[40] Under the PTK 007, any changes of the scope of contract are permitted without initiating a new tendering procedure if, among other things, these changes of the scope of works/services/supplies are brought by an event which is beyond the control of the upstream oil and gas companies and which cannot be anticipated beforehand and, for technical reasons, they constitute inseparable works to the initial scope of

---

38 *Id*, Article 38 paragraph (5) (g).

39 ee the Government Regulation of the Republic of Indonesia No. 29 of 2000 on the Construction Services dated 30 May 2000 as published in the Staatsblad (Law Gazette) No. 64 of 2010 as amended by Government Regulation of the Republic of Indonesia Number 59 of 2010, Government Regulation of the Republic of Indonesia Number 79 of 2015 and lastly amended by Government Regulation of the Republic of Indonesia Number 54 of 2016, at Article 21 (1).

40 PTK-007/SKKMA0000/2017/S0 concerning Technical Guidance for Procurement of Goods and Service in oil and gas sector ("**PTK 007**"), second book chapter VII section 2.4 & 2.5.

work.[41] In that case, the increase in price shall not exceed 10 per cent of the original contract value and shall not be larger than US$ 5,000,000 (five million United States Dollar).[42] If the additional work is assumed more than once, such caps shall apply on a cumulative basis.[43] The caps shall not apply for:

a) change of the scope of works/services/supplies which fulfils the following criteria:
    - additional works/services/supplies are required to cope with emergency or *force majeure*;
    - the granting of additional works/services/supplies meets the requirements set out by the regulations affecting the execution of the contract;
    - it is necessary for the bridging for the works/services/supplies that it must be continuously performed, and the new contract is still under the tendering process, provided that the maximum period for bridging is 1 year; and
    - it is an additional job to utilize the equipment when it is not being used but is listed down in the current contract with another upstream oil and gas company.
b) the completion of drilling activities where the increase in price shall not exceed 30 per cent of the original contract value; and
c) integrated construction work (engineering, procurement, construction, or installation), where the increase in price shall not exceed 30 per cent of the original contract value, unless it is caused by the significant change of sub-surface condition.[44]

It should be noted that any change of the scope of work can only be executed after the approval from SKK Migas.[45] In the oil and gas sector, the restriction on the change of scope of contract due to unforeseen circumstances is more rigid: (1) they must prove that the circumstance is beyond the control of the parties and cannot be anticipated beforehand and (2) they must also obtain approval from SKK Migas. It seems that under the PTK 007, fair competition is maintained during the execution of the contract and freedom of contract of the parties is limited by a stringent normative rule.

---

41 *Id*, second book chapter VII section 2.5.
42 *Id*, second book chapter VII section 2.6.
43 *Id*, second book chapter VII section 2.6.
44 *Id*, second book chapter VII section 2.6.1 to 2.6.3.
45 *Id*, second book chapter VII section 3.4.

2. Replacement of the Initial Contractor

PR 16/2018 does not provide either an explicit prohibition or permission for the replacement of an initial contractor who was appointed through a competitive procedure. PR 16/2018 only provide several conditions in relation with subcontract. Similarly, Perka LKPP 9/2018 also fails to address this issue. Lack of rules in this matter may cause the winning bidder to carry out corporate restructuring after the tender process which will lead into change in control resulting in another entity become a controlling entity in carry out the project. This may be considered as violation of fair competition principle because this practice may result in a dominant position by certain economic operator.

If we refer to the Regulation of the Head of National Public Procurement Agency Number 14 of 2012 concerning Technical Guidance for the Procurement of Government Goods and Services ("**Perka LKPP 14/2012**") which is replaced by Perka LKPP 9/2018, LKPP allows change of contractor's name resulting from a merger, consolidation, de-merger or any similar arrangement.[46] In Perka LKPP 14/2012, LKPP uses the expression "change of contractor's name" instead of "replacement of the initial contractor", which can be interpreted as not allowing the replacement of the initial contractor unless the legal personality of the initial contractor can no longer be maintained due to a merger, consolidation, or any similar transaction.

In the case of a de-merger, Indonesian Company Law defines a de-merger as a legal action taken by a company to de-merge its businesses that results in all the assets and liabilities of the company passing by operation of law to 2 (two) or more companies or a part of the assets and liabilities of the company passing by operation of law to 1 (one) or more companies.[47] Consequently, if the initial contractor demerges its entire business, all the contracts signed by the initial

---

[46] See Regulation of the Head of National Public Procurement Agency of the Republic of Indonesia No. 14 of 2012 concerning Technical Guidance for the Procurement of Government Goods and Services ("**Perka LKPP 14/2012**"), chapter II, section (A) (10) (d); chapter III, section A (10) (d); chapter IV, section A (10) (d); chapter VII, section (A) (10) (d).

[47] The Law of the Republic of Indonesia No. 40 of 2007 concerning Limited Liability Company dated 16 August 2007 as published in the Staatsblad (Law Gazette) No. 106 of 2007, article 1 (12).

contractor will be transferred by operation of law to another company. It is then acceptable to allow the new company, as the successor of the initial contractor, to continue with the execution of the public contract, unless the contract prohibits corporate restructuring. With respect to this matter, we need a regulation that prohibits corporate restructuring which is intended to circumvent any conditions or requirements under the tender documents. Therefore, it will also restrict replacement of initial contractor.

3. Extension of Time for the Completion of a Contract as a Substantial Modification

Both PR 16/2018 and Perka LKPP 9/2018 allows extension of time for the completion of a public contract only in the event of force majeure. However, Perka LKPP 14/2012 set out a list of conditions when the contracting authority can grant an extension of time to its contractor, which runs as follows:[48]

a) there are additional works to be executed by the contractor which are not included in the initial contract document, and the additional works are given in accordance with the applicable rules;
b) there are change in the design;
c) the execution of the contract is delayed due to the negligence or omission of the contracting authority;
d) the extension of time is required because of the occurrence of any problems which are beyond the control of the contractor; and/or
e) the extension of time is required because of the occurrence of *force majeure*.

Revocation of Perka LKPP 14/2012 makes extension of time for the completion of a public contract, caused by circumstances other than force majeure, cannot be granted by the contracting authority.

PTK 007 also allows an extension of the contract period if it is required, provided that the extension period shall not be longer than 2 years after the expiry of the initial contract period.[49] It should be noted that by giving a time extension for the completion of the obligations of the contractor or an extension of the contract period, the contracting authorities are modifying the economic balance of

---

48 See Perka LKPP 14/2012, *supra note* 46, chapter II, section (C) (2) (q); chapter III, section C (2) (m); chapter IV, section C (2) (p); chapter VII, section (C) (2) (n).
49 PTK 007, *supra note* 40, second book chapter VII section 2.5.

the contract in favor of the contractor. This situation may be considered as a violation of the fair competition principle. In order to ensure that the contracting authority is able to obtain the contract with the greatest value for money, revocation of Perka LKPP 14/2012 that allows extension of time in several occasions may be considered as improvement to the procurement regulations in Indonesia.

4. Specific Clause on Price Adjustment for Certain Types of Public Contract

Article 37 of PR 16/2018 stipulates that any adjustment to the contract price may be made, provided that the contract price is in a unit price, the contract period is more than 18 (eighteen) months, and the calculation method for price adjustment is clearly formulated in the initial tender document. The price adjustment clause can be invoked by the contractor starting from the thirteenth month after the execution of the contract for each of the components in the contract, excluding the component relating to profit margin, overhead cost, and unbalance unit price (*harga satuan timpang*).

Under PTK 007, the change of contract price may be allowed if the formula for the unit price adjustment is stipulated in the contract, the changes meet the requirements set out by the regulations affecting the execution of the contract, and there are specific conditions that have been declared by SKK Migas such as a decrease in the crude oil price.[50] The requirement to stipulate the formula for a price adjustment in the contract as stipulated in PR 16/2018 and PTK 007 may limit the conditions under which the contractor can invoke this review clause. Thus, it can be assumed that this rule is manifestation of fair competition principle in the execution of a public contract.

5. Force Majeure as the Reason to Modify a Public Contract

Based on freedom of contract principle, the parties are free to agree on the consequences of *force majeure* including to renegotiate the terms and conditions

[50] PTK 007, *supra note* 40, second book chapter VII section 2.4.

of contract. PR 16/2018 defines *force majeure* as an eventuality that takes place beyond the control of the parties and that cannot be anticipated by the parties, resulting in the impossibility of executing the contract.[51] In line with freedom of contract principle, PR 16/2018 allows the parties to a public contract to modify the contract in the event of *force majeure.* However, there is no limitation set out with respect to such modification. The question then arises on whether fair competition should be disregarded in the event of *force majeure*. It should be noted that in the event of *force majeure,* there is change of circumstances that frustrate the execution of the contract. In addition, the economic balances between the contractor and contracting authorities will also change. Therefore, modification of a public contract during *force majeure* shall not be considered as violation of fair competition to the extent that the *force majeure* condition cannot be avoided and confirmed by the government.

The PTK 007 also allows changes of the scope of the contract if they are required to cope with emergency or *force majeure*.[52] However, SKK Migas must approve the changes of the scope of the contract. It is understood that in the upstream oil and gas sector, SKK Migas is involved in the execution contract stage as the body who will give approval for any change of the scope of the contract. Therefore, ensuring the good governance of the procurement procedure organized by the upstream oil and gas companies.

The role of SKK Migas in the procurement system in the upstream oil and gas sector cannot be easily followed by other bodies, for instance LKPP. It will be difficult for LKPP to assess and grant approval for each of the modifications of the public contracts submitted by various contracting authorities in various industries. Nonetheless, LKPP also issued an instrument that might be used to maintain the implementation of fair competition during the execution of the contract, which is the regulation on the whistleblowing system.

---

51 PR 16/2018, *supra note* 24, at article 1 (52).

52 PTK 007, *supra note* 40, second book chapter VII section 2.5.

6. The Whistleblowing Mechanism

In order to improve the Indonesian procurement system and to ensure that such a system is free from any corruption, collusion, and unfair competition, it is necessary to strengthen the whistleblowing mechanism. Bearing in mind this objective, LKPP developed a regulation that will encourage the disclosure of any deviation from the prevailing regulation or abuse of power in the system of procurement of goods and services. LKPP set out the criteria of the reporting object in whistleblowing system as follows:[53]

a) violation of the good administration principle, including negligence in the tendering procedure;
b) unfair competition such as conflict of interest, dominant position, and collusive tendering; or
c) a criminal act such as indication of forgery, corruption, collusion and fraud.

LKPP will also provide protection for any whistleblower, including the following conditions:[54]

a) the identity of the whistleblower will be kept secret;
b) protection from any demotion or other detrimental effect upon his or her employment status;
c) protection from any physical threat including by way of mutation to another division; and
d) upon a written request from the relevant whistleblower, protection from witness and victim protection institution.

Substantial Modification Under Government Procurement Agreement

We have discussed procurement regulations in Indonesia and how the regulations restrict the implementation of freedom of contract principle to protect economic operators from unfair competition in a contract that is granted through competitive procedure. In the international level, there is Government Procurement Agreement **("GPA")** which is a multilateral agreement within the framework of the World Trade Organization, WTO, which aims mutually to open

---

53 See Regulation of the Head of National Public Procurement Agency Number 11 of 2014 concerning Whistleblowing System for the Procurement of Government Goods and Services as amended by Regulation of the Head of National Public Procurement Agency Number 1 of 2018, at article 5.

54 See *Id*, at Article 22.

and enlarge the government procurement market among its parties.[55] The first agreement, the so-called "Tokyo Round Code on Government Procurement", was signed in 1979 and came into effect in 1981. It was renegotiated and amended in 1987 and 1994 to extend the scope and coverage of the agreement. A new agreement on Government Procurement was signed in Marakesh on April 15 1994, which was then renegotiated two years after its implementation and the revised version came into effect on April 6 2014.[56] While the Revised GPA has come into effect for most parties, the GPA 1994 remains in force for those parties who are still in the process of ratifying the Revised GPA.[57]

Article IV of the Revised GPA stipulated that each Party shall accord immediately and unconditionally, to the goods and services of any other Party and to the suppliers of any other Party offering the goods and services of any party, treatment no less favorable than the treatment to the Party accords to (1) domestic goods, services and suppliers and (2) goods, services and suppliers of any other Party.[58] In addition, Article VI of the Revised GPA stipulated that each Party shall promptly publish, *inter alia*, notices or tender documentation and procedure regarding covered procurement, as well as any modifications thereof, in an officially designated media that is widely disseminated and accessible to the public.[59]

The Revised GPA does not have any specific rule on the substantial modification of a public contract. However, Article XIII (1) (c) of the Revised GPA allows a procuring entity to modify a public contract without initiating a new public tender for additional deliveries by the original supplier of goods or services which were not included in the initial procurement. This modification is allowed in situations where a change of supplier for such additional goods or services (1)

---

55 Agreement on Government Procurement, https://www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm, last visited (17-05-17).

56 *Id*.

57 Agreement on Government Procurement, https://www.wto.org/english/tratop_e/gproc_e/gpa_1994_e.htm, last visited (17-05-17).

58 Annex to the Protocol Amending the Agreement on Government Procurement, adopted on 30 March 2012 (GPA/113), article IV (1).

59 *Id*, article VI (1) (a).

cannot be made for economic or technical reasons such as the requirements of interchangeability or interoperability with existing equipment, software, services or installations procured under the initial procurement; and/or (2) would cause significant inconvenience or substantial duplication of costs for the procuring entity.[60] In addition, although the Revised GPA does not regulate itself whether a substantial modification of a public contract can be made, the Revised GPA provides in Article XV (5) that a procuring entity shall award the contract to the supplier whom the entity has determined as capable of fulfilling the terms of the contract, and who, based solely on the evaluation criteria specified in the tender documentation, has submitted the most advantageous tender, or where price is the sole criterion, the supplier who offers the lowest price.[61] From this provision, it can be concluded that a modification of a public contract shall require a new tendering procedure if such a modification would provide the opportunity to the unsuccessful tenderer to submit the most advantageous tender. Otherwise, such a modification may infringe upon the principle of non-discrimination and transparency under Articles IV and VI of the Revised GPA.

Conclusion

Freedom of contract is general principle in contract law. Nevertheless, the application of this principle must be limited in the case of a public contract. It must be noted that, in public procurement sector, a competitive procurement procedure is required to ensure the availability of quality goods and services at affordable prices, which will in turn have an impact on improved public services. Since a public contract is awarded through a competitive procurement procedure, it is important to maintain the principle of fair competition among the potential tenderers and transparency for the economic operators who have an interest in participating in the procurement procedure. In practice, the parties to a public contract often forget to observe the rule of fair competition between economic operators during the execution of a public contract. In turn, it will be detrimental

60 *Id*, article XIII (1) (c).
61 *Id*, article XV (5).

both to the government and to the economic operators. The contracting authority will fail to obtain the contract with the best value for money, which in turn will reduce the efficient use of public funds. On other side, the economic operators' right to be treated fairly is infringed. Therefore, procurement regulations must be drafted in a way that it is not easy to modify the terms of conditions of the public contract that is included in the document governing the award procedure.

Although Indonesian procurement regulation has been drafted in a very strict manner in relation with modification of a public contract, Indonesian procurement regulations may still be improved. For instance, there may be a need to prohibit substantial modification to a public contract although the increase in price is less than 10% (ten percent) of the initial contract price. Referring to explanation on GPA, modification may be considered material if it introduces conditions which would allow the admission of other candidates or acceptance of other tenderers if they had been part of the initial tender documents. By prohibiting substantial modification, government is able to protect public interest and maintain fair competition principle at the same time. In addition, it is necessary to add several rules with regards to replacement of initial contractor to avoid corporate restructuring that may result in dominant position by one economic operator.

Bibliography

Books:

A. Semple, A Practical Guide to Public Procurement, Oxford University Press, Oxford, 2015.

A. S. Hartkamp et al., Contract Law in the Netherlands, Kluwer Law International, The Netherlands, 2011.

S. Arrowsmith and P. Kunzlik, Social and Environmental Policies in EC Procurement Law: New Directives and New Directions, Cambridge University Press, Cambridge, 2009.

S. Arrowsmith, The Law of Public and Utilities Procurement Regulation in The EU and UK, 3rd ed., Vol. I, London, 2014.
S. Ramli, Bacaan Wajib Mengatasi Aneka Masalah Teknis Pengadaan Barang/Jasa Pemerintah, Visimedia, Jakarta, 2014.

Articles:
G.M. Racca and R.C. Perin, Material Amendments of Public Contracts During Their Term: From Violations of Competition to Symptoms of Corruption, 8 EPPPL, 2013.
G.M. Racca, *et al*., Competition in the Execution Phase of Public Procurement, 41 Public Contract Law Journal, 2011.
O. Dekel, Modification of A Government Contract Awarded Following a Competitive Procedure, 38 Public Contract Law Journal, 2009.
R. A. Suryo and A.M. Ulfa, Teori Kontrak dan Implikasinya Terhadap Regulasi Pengadaan Barang dan Jasa Pemerintah, 3 Jurnal Pengadaan, 2013.
R. D. Olivera, Modification of Public Contracts Transposition and Interpretation of the New EU Directives, 10 EPPPL, 2015.
S. N. Bahagia, Sistem Pengadaan Publik dan Cakupannya, 1 Senarai Pengadaan Barang/Jasa Pemerintah, 2011.

Compilations:
G.M. Racca and R.C. Perin, Material changes in contract management as symptoms of corruption: a comparison between EU and U.S. procurement systems, in G.M Racca and C.R. Yukins (Ed.), Integrity and Efficiency in Sustainable Public Contracts Balancing Corruption Concerns in Public Procurement Internationally, Bruxelles, 2014.
F. J. Vazquez Matilla, The Modification of Public Contract: an obstacle to transparency and efficiency, in G.M Racca and C.R. Yukins (Ed.), Integrity and Efficiency in Sustainable Public Contracts Balancing Corruption Concerns in Public Procurement Internationally, Bruxelles, 2014.

Legislation:
Law of the Republic of Indonesia No. 5 of 1999 concerning Anti-Monopoly and Unfair Competition.
Law of the Republic of Indonesia No. 40 of 2007 concerning Limited Liability Company.
Law of the Republic of Indonesia Number 2 of 2017 concerning Construction Services.
Government Regulation of the Republic of Indonesia No. 29 of 2000 on the Construction Services as amended by Government Regulation of the Republic of Indonesia Number 59 of 2010, Government Regulation of the Republic of Indonesia Number 79 of 2015 and lastly amended by Government Regulation of the Republic of Indonesia Number 54 of 2016.
Presidential Regulation of the Republic of Indonesia Number 54 of 2010 on the Procurement of Government Goods and Services as amended by Presidential Regulation of the Republic of Indonesia Number 35 of 2011,

Presidential Regulation of the Republic of Indonesia Number 70 of 2012, Presidential Regulation of the Republic of Indonesia Number 172 of 2014 and lastly Presidential Regulation of the Republic of Indonesia Number 4 of 2015.

Regulation of the Head of National Public Procurement Agency of the Republic of Indonesia No. 14 of 2012 concerning Technical Guidance for the Procurement of Government Goods and Services.

Regulation of the Head of National Public Procurement Agency No. 11 of 2014 concerning Whistleblowing System for the Procurement of Government Goods and Services as amended by Regulation of the Head of National Public Procurement Agency Number 1 of 2018.

Regulation of the Head of National Public Procurement Agency of the Republic of Indonesia No. 9 of 2018 concerning Technical Guidance for the Procurement of Government Goods and Services.

PTK-007/SKKMA0000/2017/S0 concerning Technical Guidance for Procurement of Goods and Service adopted on 30 May 2017.

Website:

Frequently Asked Question of LKPP, *https://www.scribd.com/document/248537528/tanya-jawab-pengadaan-lkpp-1-pdf*.

Agreement on Government Procurement, *https://www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm.*

Agreement on Government Procurement, *https://www.wto.org/english/tratop_e/gproc_e/gpa_1994_e.htm.*

Badan Pemeriksa Keuangan, Ikhtisar Hasil Pemeriksaan Semester I Tahun 2016, available at *http://www.bpk.go.id/assets/files/ihps/2016/I/ihps_i_2016_1475566035.pdf*.